

**DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 99-0117
Use Tax
For Tax Years 1995 through 1997**

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ISSUES

I. Use Tax—Tangible personal property

Authority: IC 6-2.5-3-2; IC 6-2.5-5-8

Taxpayer protests imposition of use tax on tangible personal property.

II. Use Tax—Returnable Containers

Authority: IC 6-2.5-5-9; 45 IAC 2.2-5-16

Taxpayer protests imposition of use tax on returnable shipping containers.

III. Tax Administration—Negligence Penalty

Authority: IC 6-8.1-5-4; 45 IAC 15-11-2

Taxpayer protests imposition of a ten percent (10%) negligence penalty.

STATEMENT OF FACTS

Taxpayer manufactures parts for the automotive industry. During the audit period, taxpayer bought tangible personal property and other equipment from out-of-state suppliers. The Department assessed use tax on these transactions and a ten percent (10%) negligence penalty. Taxpayer protests the assessments and penalty. Further facts will be supplied as required.

I. Use Tax—Use Tax Assessments

DISCUSSION

Taxpayer protests the Department's assessments of use tax on various items. The Department assessed use tax on tangible personal property that taxpayer acquired from vendors and then transferred to its own customer. Taxpayer states that the tangible personal property was located outside of Indiana when the sales occurred. Taxpayer also argues that much of the assessments pertain to equipment (tangible personal property) for research and development and is exempt from Indiana use tax under the resale exemption. The relevant statute for the resale exemption is IC 6-2.5-5-8, which states in relevant part:

Transactions involving tangible personal property are exempt from the state gross retail tax if the person acquiring the property acquires it for resale, rental, or leasing in the ordinary course of his business without changing the form of the property.

The Department assessed those of taxpayer's accounts which included costs of samples, including prototype samples from which tooling would be produced for the manufacture of products. The fact that some of these accounts were for research and development costs does not mean that they are exempt from use tax. The resale exemption applies to tangible personal property acquired for resale, rental or lease in the ordinary course of business without changing the form of the property.

During the audit, taxpayer explained that copies of the invoices received by taxpayer were generally forwarded to taxpayer's parent companies, which may or may not reimburse taxpayer for these costs. Taxpayer was unable to produce documentation establishing which, if any, costs were for transactions involving tangible personal property acquired for resale, rental, or leasing in the ordinary course of its business without changing the form of the property.

At the time of the audit, taxpayer was unable to provide records establishing the location and ownership of the tangible personal property. As IC 6-2.5-3-2(a) explains:

An excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction.

The Department based its assessments on the best information available. As part of this protest, taxpayer has now provided the Department with documentation showing that approximately eighty-five percent (85%) of the tangible personal property in question was located out of state. Unfortunately, the documentation does not cover the audit period, but rather it covers years after the audit period.

Taxpayer has not provided documentation showing that the requirements of IC 6-2.5-5-8 (the resale exemption) were satisfied. The documentation provided did not cover the audit period. Therefore, the tangible personal property in question does not qualify for the resale exemption.

FINDING

Taxpayer's protest is denied.

II. Use Tax—Returnable Containers

DISCUSSION

The Department also assessed use tax on shipping containers owned by taxpayer and used by various suppliers to transport goods to the taxpayer's manufacturing plant. Taxpayer states that these containers either are owned by its customer or are exempt from use tax as returnable containers. Taxpayer refers to IC 6-2.5-5-9, which states:

- (a) As used in this section, "returnable containers" means containers customarily returned by buyer of the contents for reuse as containers.
- (b) Sales of returnable containers are exempt from the state gross retail tax if the transaction constitutes selling at retail as defined in IC 6-2.5-4-1 and if the returnable containers contain contents.
- (c) Sales of returnable containers are exempt from the state gross retail tax if the containers are transferred empty for the purpose of refilling.
- (d) Sales of wrapping material and empty containers are exempt from the state gross retail tax if the person acquiring the material or containers acquires them for use as nonreturnable packages for selling the contents that he adds.

Taxpayer believes that the containers qualify for this exemption. The Department refers to 45 IAC 2.2-5-16, which states in part:

- (d) Application of general rule.
 - (1) Nonreturnable wrapping material and empty containers. To qualify for this exemption, nonreturnable wrapping materials and empty containers must be used by the purchaser in the following way:
 - (A) The purchaser must add contents to the containers purchased; and
 - (B) The purchaser must sell the contents added.
 - (2) Returnable containers sold at retail with contents. To qualify for this exemption, the returnable containers must be:
 - (A) Sold in a taxable transaction of a retail merchant constituting selling at retail; and
 - (B) Billed as a separate charge by the retail merchant to his customer. If there is a separate charge for such containers, the sale of the container is exempt from tax under this regulation [45 IAC 2.2].
 - (3) Returnable containers sold empty. To qualify for this exemption the returnable container must be resold with the purpose of refilling. The sale of returnable containers to the original or first user thereof is taxable.

The exemption provided by IC 6-2.5-5-9 establishes that the initial purchaser of the containers, in this instance the taxpayer, pays tax on the initial acquisition of the containers. After that,

additional sales of returnable containers are exempt, provided the sales meet the requirements of 45 IAC 2.2-5-16(d)(2)(B). In either circumstance, the exemption is not available since taxpayer has not provided documentation to establish that the returnable containers are billed as a separate charge in a retail transaction, as required by 45 IAC 2.2-5-16(d)(2)(B). As to taxpayer's alternative argument, taxpayer has not provided documentation establishing that the containers belong to its customer. Therefore, the returnable shipping containers are properly subject to use tax.

FINDING

Taxpayer's protest is denied.

III. Tax Administration—Negligence Penalty

DISCUSSION

Taxpayer protests the imposition of a ten percent (10%) negligence penalty. Taxpayer states that the assessments in question are insignificant when compared to its total business activity and the amount of tax correctly paid. The relevant regulation is 45 IAC 15-11-2(b), which states:

“Negligence” on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable person. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed on it by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules, and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

Taxpayer believes that its facts and circumstances warrant dismissal of the negligence penalty. The Department refers to IC 6-8.1-5-4(a), which states:

Every person subject to a listed tax must keep books and records so that the department can determine the amount, if any, of the person's liability for that tax by reviewing those books and records. The records referred to in this subsection include all source documents necessary to determine the tax, including invoices, register tapes, receipts, and canceled checks.

Also, IC 6-8.1-5-4(c) states:

A person must allow inspection of the books and records and returns by the department or its authorized agents at all reasonable times.

In this case, taxpayer failed to keep records for the auditor to review in order to determine the amount, if any, of the taxpayer's liability. While taxpayer was eventually able to produce some

documentation, which may partially supports its position, this documentation was not available until it was provided in this protest. Taxpayer failed to comply with the record keeping requirement of IC 6-8.1-5-4, and was therefore negligent as described in 45 IAC 15-11-2(b). If this documentation had been available during the audit, much of the time and effort for taxpayer and the Department could have been saved. Therefore, the assessments will be subject to the ten percent (10%) negligence penalty.

FINDING

Taxpayer's protest is denied.

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